United States Courts
Southern District of Texas
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UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

AMALGAMATED BANK, as Trustee for LONGVIEW COLLECTIVE INVESTMENT FUND, LONGVIEW CORE BOND INDEX FUND and CERTAIN OTHER TRUST ACCOUNTS, Individually and On Behalf of All Other Similarly Situated.	§	
v.	§	
KENNETH L. LAY, JEFFREY K. SKILLING, ANDREW S. FASTOW, RICHARD A. CAUSEY, JAMES V. DERRICK, JR., CLIFFORD BAXTER, MARK A. FREVERT, STANLEY C. HORTON, KENNETH D. RICE, RICHARD B. BUY, LOU L. PAI, ROBERT A. BELFER, NORMAN P. BLAKE, JR., RONNIE C. CHAN, JOHN H. DUNCAN, WENDY L. GRAMM, ROBERT K. JAEDICKE, CHARLES A. LEMAISTRE, JOE H. FOY, JOSEPH M. HIRKO, KEN L. HARRISON, MARK E. KOEINIG, STEVEN J. KEAN, REBECCA P. MARK-JUSBASCHE, MICHAEL S. MCCONNELL, JEFFREY MCMAHON, CINDY K. OLSON, J. MARK METTS, JOSEPH W. SUTTON and ARTHUR ANDERSEN, LLP.	§	Civil Action No. H-01-~~4198~~ 3624 CLASS ACTION

DEFENDANTS' JOINT BRIEF REGARDING
LIMITS ON THE DISTRICT COURT'S EQUITABLE POWER
TO GRANT A PREJUDGMENT RESTRAINT ON DEFENDANTS' ASSETS

TO THE HONORABLE LEE H. ROSENTHAL:

In *Grupo Mexicano*, the Supreme Court recognized that prejudgment seizure of assets was a "nuclear weapon" that might destroy the ability of a litigant to defend himself or herself. *See Grupo Mexicano de Desarrollo, S.A. v. Alliance Bond Fund,* 527 U.S. 308, 332 (1999). The Court

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held that the "equitable powers conferred by the Judiciary Act of 1789 did not include the power to create remedies previously unknown to equity jurisprudence." *Id.* at 332. The *Grupo Mexicano* Court thus made clear that the federal courts have no general equitable authority to issue a prejudgment injunction restraining assets where "no lien or equitable interest is claimed." *Id.* at 310 (emphasis added). On that basis the Supreme Court denied, expressly, what Plaintiff seeks to obtain here: A prejudgment seizure of assets to secure a money judgment.

Plaintiff's demand for injunctive relief and seizure is not authorized here because Plaintiff asserts no cognizable claim to an "equitable interest" in the assets it seeks to enjoin. *Id.* First, Plaintiff has failed to allege a cognizable claim for equitable relief. Second, as is demonstrated below, Plaintiff has not alleged--because it cannot do so--that its claim gives it an equitable interest in Defendants' assets. No matter how many times Plaintiff endeavors to recast its claims, it cannot satisfy the fundamental requirement of a claim for an equitable interest in the Defendants' assets; namely, a showing that each and every one of the defendants, individually, is in possession of a particular plaintiff's property. *See United States v. Benitez*, 779 F.2d 135, 139 (2d Cir. 1985). Indeed, the very foundation of all equitable remedies creating an equitable interest in property is that the plaintiff seeking the equitable relief is able to show that the defendant has been unjustly enriched at the expense of the plaintiff. *See* RESTATEMENT (THIRD) OF RESTITUTION AND UNJUST ENRICHMENT § 4 (Discussion Draft, 2000) (emphasis added). As is demonstrated below, Plaintiff can make no such showing here.

Finally, the allegations pleaded in support of Plaintiff's statutory claims do not make out a claim for equitable relief, and the statutes themselves do not authorize, by their terms, the award of a prejudgment seizure. Thus, Plaintiff's attempt to cure its inability to plead the requirements for

equitable relief by characterizing its statutory claims as "equitable" in nature fails because: i) such a characterization cannot expand the scope of the Court's general equitable powers; and ii) Plaintiff's statutory claims are legal in nature, not equitable, and, thus, Plaintiff's characterizations are wrong in the first instance.

Accordingly, under the holdings of both *Grupo Mexicano* and *Deckert v. Indep. Shares Corp.*, 311 U.S. 282 (1940), this Court lacks the power to grant Plaintiff a prejudgment seizure of the Defendants' assets.[1]

I.

The Meaning of *Grupo Mexicano*

In *Grupo Mexicano*, the Supreme Court upheld the "well-established general rule that a judgment establishing the debt was necessary before a court of equity would interfere with the debtor's use of his property." 527 U.S. at 321. The Court, relying on its earlier opinion in *DeBeers Consol. Mines, Ltd. v. United States*, observed that any disappointed plaintiff might otherwise seek relief of the type sought here:

> [I]t is difficult to see why a plaintiff in any action for a personal judgment in tort or contract may not, also, apply to the chancellor for a so-called injunction sequestrating his opponent's assets pending recovery and satisfaction of a judgment in such law action. No relief of this character has been thought justified in the long history of equity jurisprudence.

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[1]Per the Court's instructions at the hearing on December 7, this joint brief by Defendants addresses only the Court's authority to enter a prejudgment injunction restraining Defendants' assets. In the unlikely event that the Court were to decide that it has such authority, further briefing and evidence would be necessary to determine whether such authority should be exercised to provide the relief requested here.

While Plaintiff's counsel made a number of generic, unsubstantiated allegations to this Court at the December 7 hearing, which Defendants vigorously dispute, Defendants understand that the Court does not contemplate addressing these issues in this joint brief. Defendants also understand that, should the Court determine that it has the power to enter the relief requested, the Court will nonetheless expect to receive additional briefing on the following subjects: (a) the effect of the automatic stay in bankruptcy on the continued pendency of this action; and (b) whether the Private Securities Litigation Reform Act permits Plaintiff to obtain the relief it has demanded in the absence of compliance with the lead plaintiff and dismissal procedures set forth in the Act.

325 U.S. 212, 222-23 (1945) (emphasis added).[2]

A.

The Narrow "Equitable Interest" Exception

The Court in *Grupo Mexicano* noted that in its earlier decision of *Deckert v. Indep. Shores Corp.*, § U.S. 282 (1940), a narrow exception to this rule was recognized where a claim for equitable relief was stated:

> [In *Deckert*] we concluded that the bill stated a cause of action for the equitable remedies of rescission of the contracts and restitution of the consideration paid, and that the preliminary injunction was a reasonable measure to preserve the status quo pending final determination of the questions raised by the bill. *Deckert* is not on point here because, as the Court took pains to explain, the bill stated a cause of action for equitable relief.

Grupo Mexicano, 527 U.S. at 325 (emphasis added). The Court concluded, therefore, that injunctive relief (such as a prejudgment seizure) is not available where "no lien or equitable interest is claimed" in the defendant's property sought to be restrained. *Id.* at 310.

The question to be decided, therefore, is simply this: Has Plaintiff alleged a claim for equitable relief of a type that was "traditionally accorded by courts of equity," *Id.* at 318. For the reasons stated below, it has not.

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[2]The Fifth Circuit has long rejected the authority of a district court under its general equitable powers to issue a prejudgment order freezing a defendants' assets in order to protect the future utility of a potential judgment for damages. *See In re Fredeman Litigation*, 843 F.2d 821, 824 (5th Cir. 1988)("The general federal rule of equity is that a court may not reach a defendant's assets unrelated to the underlying litigation and freeze them so that they may be preserved to satisfy a potential money judgment"), *citing DeBeers Consolidated Mines v. United States*, 325 U.S. 212 (1945). Just as in the *Fredeman* case, Plaintiff here does "not ultimately seek return of any particular asset or fund that the interim injunction might secure or that has been used to violate the [RICO] statute . . . " 843 F.2d at 825, and therefore invites this court Court to commit error by entering such an injunction in violation of longstanding Fifth Circuit precedent."

B.

Prejudgment Seizure Requires Proof of an "Equitable Interest" in Property.

Grupo Mexicano, like the earlier decision in *Deckert*, makes clear that a plaintiff has no valid "equitable interest" in a defendant's property unless: (a) the plaintiff alleges facts making out a claim in equity; and (b) the equitable claim itself creates an equitable right in favor of the plaintiff in the defendant's property or assets. In the words of the case invoked by Plaintiff:

> To apply these principles, we must begin with an analysis of the claims in the suit to determine whether they seek cognizable relief in equity involving assets of the defendant.

United States ex rel. Rahman v. Oncology Assoc., P.C., 198 F.3d 489, 497 (4th Cir. 1999) (emphasis added). *Accord F.T. Int'l, Ltd. v. Mason*, 2000 WL 1479819, * 1 (E.D. Penn. October 5, 2000) ("a plaintiff may obtain a prejudgment freeze on a defendant's assets only if he has asserted a cognizable equitable claim [and] has demonstrated a sufficient nexus between that claim and specific assets of the defendant which are the target of the injunctive relief.").[3] Here, Plaintiff fails this threshold test

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[3] The cases cited by Plaintiff in support of its claim for prejudgment seizure are not only predominantly pre-*Grupo Mexicano,* but are also almost exclusively cases involving the government as plaintiff, necessitating an entirely different analysis from a case such as this one where only private interests are at stake. *Rahman* 198 F.3d at 497 (emphasis in the original) ("we must recognize that when interim equitable relief is authorized *and the public interest is involved*, the doctrine applies that courts of equity may, and frequently do, go much further both to give and withhold relief in furtherance of the public interest than they are accustomed to go when only private interests are involved.").

Courts since *Grupo Mexicano* have consistently recognized the requirement that a private plaintiff must allege a cognizable claim in equity, having a sufficient nexus to the assets sought to be enjoined, before a court may use its injunctive power to enjoin a defendant's assets pre-judgment. *See, e.g., Rahman*, 198 F.3d 489 (4th Cir, 1999) (creditor made cognizable claim for constructive trust); *Wishnatzki v. H.P. Island-Wide*, 2000 WL 1610790 (S.D.N.Y. 2000) (plaintiff asserted equitable interest in funds as beneficiaries of a statutory trust); *F.T. Int'l, Ltd. v. Mason*, 2000 WL 1514881 (E.D. Pa. October 11, 2000) (plaintiff claiming unjust enrichment and constructive trust).

Similarly, numerous courts following *Grupo Mexicano* have refused to enjoin assets of a defendant in instances where a plaintiff did not have an equitable interest and could not assert a cognizable claim in equity. *See, In re Seatco*, 259 B.R. 279 (N.D. Tex. 2001) (deciding that the court "cannot grant prejudgment relief" on a party's tort and contract claims); *Traffix, Inc. v. Talk.com*, 2001 WL 123724 (S.D.N.Y.)(court could not enter an injunction because the plaintiff "does not hold any security interest or lien" against the defendant); *1800 Postcards, Inc. v. Morel*, 153 F.Supp.2d 259 (S.D.N.Y. 2001) (court held it lacked authority to freeze defendants' "unencumbered assets" on the basis of plaintiff's fraud claim); *Contichem LPG v. Parsons Shipping Co., Ltd.*, 229 F.3d 426, 430 (2d Cir. 2000) ("As a preliminary matter,

because it does not "seek cognizable relief in equity involving the assets of the defendant." *Rahman*, 198 F.3d at 497.

The only "cognizable relief in equity" that a federal court can grant pursuant to its general equitable powers are those forms of relief that "had been devised and were being administered by the English Courts of Chancery" as of 1789. *Grupo Mexicano*, 527 U.S. at 318, 332. This is so because the federal courts' general equitable powers arise solely out of the Judiciary Act of 1789 and are subject to well-defined limits:

> [T]he equity jurisdiction of the federal courts is the jurisdiction in equity exercised by the High Court of Chancery in England at the time of the adoption of the Constitution and enactment of the Judiciary Act of 1789.
>
> The jurisdiction thus conferred is an authority to administer in equity suits the principles of the system of judicial remedies which had been devised and was being administered by the English Court of Chancery at the time of the separation of the two countries.
>
> [T]he equitable powers conferred by the Judiciary Act of 1789 did not include the power to create remedies previously unknown to equity jurisprudence.

Grupo Mexicano, 527 U.S. at 318, 332 (emphasis added, citations and quotations omitted). As the *Grupo Mexicano* opinion goes on to explain, "the prerequisites for obtaining an equitable remedy . . . depend on traditional principles of equity jurisdiction." *Id.* at 318-319 (emphasis added, quotations omitted).

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we agree with the district court's determination that because Contichem did not have a judgment against Parsons, the court had no equitable power to issue a preliminary injunction preventing any entity from disposing of Parson's assets...").

As is set out in the next section, Plaintiff has not pleaded and cannot prove each of the "prerequisites" of any cognizable relief in equity related to the assets it seeks to restrain and, therefore, its motion must fail.

C.

Plaintiff Does Not Assert Cognizable Claims for Relief in Equity Involving Defendant's Assets

The only cognizable relief in equity that Plaintiff purports to pursue in this lawsuit is the imposition of a constructive trust over the proceeds of the Defendants' alleged sales of Enron common stock during the class period. However, Plaintiff has not alleged and cannot prove the most basic of the traditional "prerequisites" for the imposition of a constructive trust: the tracing of the claimant's property into the hands of the alleged wrongdoer.

Plaintiff's theory is that the Defendants' sales of Enron stock during the class period were fraudulent, and that Defendants therefore hold the proceeds of those sales in constructive trust on behalf of the purchasers of their shares. However, "[i]t is hornbook law that before a constructive trust may be imposed, a claimant to a wrongdoer's property must trace its own property into a product in the hands of a wrongdoer." *United States v. Benitez*, 779 F.2d 135, 139 (2d Cir. 1985) (emphasis added). *Accord In re Kennedy & Cohen, Inc.*, 612 F.2d 963, 966 (5th Cir. 1980) (emphasis added) ("Under federal law [governing constructive trusts], plaintiffs must be able to trace their funds into an identifiable trust in the hands of the trustee.").

Thus, Plaintiff is entitled to the equitable remedy of a constructive trust if, and only if, it can trace the exact shares it purchased directly to the exact shares sold by the Defendants (i.e. it can trace

its own property into the hands of the Defendants). Neither Plaintiff nor the members of the putative Plaintiff class can meet this test.

Plaintiff makes no allegation that either it, or any individual member of the putative Plaintiff class, can trace their property into the hands of the Defendants. This is so because no such allegation could ever be proven. Enron shares were actively traded in the securities market in enormous daily volumes during the class period. Given the structure of the equities markets, the length of the class period, the number of shares sold by the individual Defendants relative to the total shares sold on any given day, and the manner in which shares of large corporations such as Enron are traded, it is simply impossible to match any individual sale of shares with any individual purchase. *See* Guth Declaration (Exh. "A") at 2-4. Because it is impossible for Plaintiff, or any individual member of the putative class, to trace their own property into the hands of any of the Defendants, neither Plaintiff nor any member of the Plaintiff class is entitled to the imposition of a constructive trust against the assets of any of the Defendants. *See, e.g., In re "Ronfin" Series C Bonds Security Interest Litigation*, 182 F.3d 366, 371 (5th Cir. 1999) (refusing to impose an equitable lien where the property was not distinguished from the defendant's general assets and where plaintiff had an adequate remedy at law.).

Plaintiff's failure to plead or prove that any of its funds are in the hands of Defendants also precludes other recognized claims in equity that could give Plaintiff an "equitable interest" in Defendants' assets. The foundation of all remedies that create an equitable interest in property or assets -- including rescission, constructive trust, subrogation, and equitable lien[4] -- is that the plaintiff

[4]RESTATEMENT (THIRD) OF RESTITUTION AND UNJUST ENRICHMENT § 4 cmt. (Discussion Draft, 2000) ("In broadest outline, restitution works by giving the plaintiff either a money judgment; proprietary rights in some specific property or fund; or a combination of the two. Remedies that vindicate a claimant's 'proprietary rights' constitute an

seeking the equitable relief is able to show that the defendant has been unjustly enriched at the expense of the plaintiff.[5] *See* RESTATEMENT (THIRD) OF RESTITUTION AND UNJUST ENRICHMENT § 4 (Discussion Draft, 2000) (emphasis added) ("The function of remedies in restitution is to prevent or redress the unjust enrichment of one or more persons at the expense of the plaintiff.").

Thus, because Plaintiff cannot plead or prove that its assets have been wrongfully obtained by any of the Defendants, it has no claim for "cognizable relief in equity involving the assets of the defendant" and, therefore, no "equitable interest" in the assets it seeks to enjoin. *Rahman*, 198 F.3d at 497. And because Plaintiff has no "equitable interest" in the assets it seeks to enjoin, the Court has no authority under its general equitable powers to grant the relief requested here by Plaintiff. *Grupo Mexicano*, 527 U.S. at 333.

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extensive category of relief, employing restitution's most distinctive remedial tools. Under this heading are classified an order restoring plaintiff to possession of his own property (as in cases of rescission and specific restitution); an order recognizing plaintiff's equitable ownership of property to which defendant has legal title (as in cases of constructive trust); and an order permitting the satisfaction of plaintiff's claims out of identifiable assets in preference to competing creditors (as in cases of subrogation and equitable lien.).

[5]After the December 7 hearing, Plaintiff hastily amended its Complaint to add cursory requests for an accounting, disgorgement, restitution, and rescission. Plaintiff pleaded no new facts to support these new requests for relief. These claims for equitable relief fail for the same reason as all of Plaintiff's others, because Plaintiff cannot allege, much less prove, that any of the Defendants has been unjustly enriched at the expense of Plaintiffs. *See* RESTATEMENT (THIRD) OF RESTITUTION AND UNJUST ENRICHMENT § 4 (Discussion Draft, 2000). Defendants note that this amended complaint is of such recent vintage that it has not yet even been served on all of their counsel. Consequently, Defendants respectfully request that they be given the opportunity to supply the Court with additional briefing to the extent that the Court believes the amendment raises issue not disposed of herein.

II.

Plaintiff's Federal Securities Claims Provide the Court No Additional Power to Grant the Requested Relief

A.

No Express Statutory Right to Prejudgment Restraint of Assets

Plaintiff's complaint purports to state causes of action against the Defendants for violations of sections10(b), 20(a), and 20A of the Exchange Act and sections 11 and 15 of the Securities Act. None of these statutes expressly authorizes a prejudgment restraint on a defendant's assets in favor of a plaintiff claiming under any of them.[6] *See infra* at Section II(D). This Court lacks the power to expand the scope of the securities acts by reading into them remedies not provided by the statutes themselves. "We find our role limited when the issue is the scope of conduct prohibited by the statute. That issue is our concern here, and we adhere to the statutory text in resolving it." *Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164, 187-88 (1994) (citations omitted) (emphasis added). Here, the statutes invoked by Plaintiff contain not a single provision that entitles Plaintiff to the equitable relief sought.

B.

Section 27 Does Not Expand the Scope of the Court's General Equitable Powers.

Section 27 does not give Plaintiff any cause of action or the right to any equitable remedy, nor does it create or expand any substantive rights:

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[6]Congress has demonstrated its ability to create statutory remedies providing for prejudgment restraints on assets in those circumstances where it considers them justified. *See* 15 U.S.C. §§ 77h-1, 78u-3 (authorizing SEC to enter temporary orders against brokers, dealers, investment companies and others restraining assets in order to prevent dissipation of assets). That it has chosen to include no such remedy in the provisions invoked by Plaintiff is dispositive, under *Central Bank*, of the question whether those remedies are available under the statutes.

> The district courts of the United States . . . **shall have exclusive jurisdiction** of violations of this chapter or the rules and regulations thereunder, and **of all suits in equity and actions at law** brought to enforce any liability or duty created by this chapter or the rules and regulations thereunder.

15 U.S.C. § 78aa (emphasis added).

Plaintiff argues that Section 27 confers an independent right to an equitable remedy, presumably based on the mere presence of the word "equity" in that Section. That argument ignores the jurisdictional context in which the word is used and the effect on Section 27 of the merger of law and equity in the Federal Rules of Civil Procedure.

Enacted in 1934, Section 27 maintained the distinction then recognized between actions at law and suits in equity. The Federal Rules of Civil Procedure, adopted in 1937, abolished the law/equity distinction: "Reference to actions at law or suits in equity in all statutes should now be treated as referring to the civil action prescribed in these rules." *See* Fed. R. Civ. P. 2 adv. cmt. note 2 (1937). Thus, the reference to equity in Section 27 represents Congress's effort to ensure completeness of federal court jurisdiction over actions, both private and governmental, under the Securities Exchange Act in a time when there existed the possibility of separate jurisdiction over "actions at law" and "suits in equity." *See Touche Ross & Co. v. Redington*, 442 U.S. 560, 577 (1979). As the Supreme Court held:

> Section 27 grants jurisdiction to the federal courts and provides for venue and service of process. It creates no cause of action of its own force and effect; it imposes no liabilities. **The source of plaintiffs' rights must be found, if at all, in the substantive provisions of the 1934 Act which they seek to enforce, not in the jurisdictional provision.**

Id. at 577 (emphasis added).

As explained in the prior section, none of the substantive provisions that Plaintiff seeks to enforce provide for an equitable remedy. Moreover, *Touche Ross* affirmed that "generalized

references to the 'remedial purposes' of the 1934 Act will not justify reading a provision more broadly than its language and the statutory scheme reasonably permit." *Id.* In doing so, the Court effectively limited to its facts the earlier decision in *J.I. Case & Co. v. Borak*, 377 U.S. 426 (1964), a decision upon which Plaintiff places heavy reliance. The Supreme Court also rejected in *Central Bank* the notion that federal courts may imply remedies in the securities laws where none exist. *See Central Bank*, 511 U.S. at 187-88.

This clear Supreme Court authority establishes that Section 27 means only that the court may use its otherwise available general equitable powers, as conferred by the Judiciary Act of 1789, in a case arising under the Exchange Act. *SEC v. Texas Gulf Sulphur Co.*, 446 F.2d 1301, 1307 (2nd Cir. 1971) (emphasis added) ("§ 27 of the Act confers general equitable power upon the district courts.").[7] Section 27 does not mean (as Plaintiff suggests) that a plaintiff bringing claims under the Exchange Act is somehow entitled to equitable relief that is either untethered to traditional equitable principles or that is granted despite the fact that the plaintiff has neither pleaded nor proved the traditional "prerequisites for obtaining an equitable remedy." *Grupo Mexicano*, 527 U.S. at 318-19.[8]

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[7] *Texas Gulf Sulphur* is the case cited in Plaintiff's Application on the scope and meaning of Section 27. *See* Application at 12.

[8] Plaintiff has cited no case, decided after *Grupo Mexicano*, in which a federal court has held that it had the power to issue a prejudgment restraint on assets in a case arising under the Exchange Act--despite the plaintiff's failure to plead or prove all of the traditional "prerequisites" for the equitable remedy that it sought to invoke. *SEC v. Brooks*, 1999 WL 493052 (N.D. Tex. July 12, 1999), the case on which Plaintiff relies, is not to the contrary. Although the court in *Brooks* did issue a prejudgment restraint on assets in favor of the SEC, the court's opinion does not cite or discuss *Grupo Mexicano*, nor does it consider or discuss the question whether the SEC had stated a claim for equitable relief giving rise to an "equitable interest" in the assets sought to be enjoined, as required by *Grupo Mexicano*. This omission is no doubt due in whole or in part to fact that: i) the court entered its original order freezing assets on June 10, 1999, one week before the Supreme Court's decision in *Grupo Mexicano* was announced, *id.* at * 6; ii) the defendant made no response to the SEC's application for injunction, *id.* at * 1; iii) the opinion cited by Plaintiff was issued less than four weeks after *Grupo Mexicano*; iv) "When asked what he would tell a federal judge who asked where the funds were being maintained, [defendant] stated, 'I'll tell him to f--- himself.'" *Id.* at * 3; and v) the party seeking the restraint was a government actor. No case decided after *Brooks* has cited it as support for the entry of a prejudgment seizure of assets.

Plaintiff's assertion that it is entitled to equitable relief also runs directly counter to the Supreme Court's holding in *Deckert*. In *Deckert*, the plaintiff sought a prejudgment seizure of assets in a case under Section 12(2) of the Securities Act. *Deckert*, 311 U.S. at 287-88. The question presented was whether the district court was entitled to make use of its general equitable powers to grant such relief. *Id.* In deciding the threshold question, the *Deckert* court explained that:

> the [Securities] Act as a whole indicates an intention to establish a statutory right which the litigant may enforce in designated courts by such legal or equitable actions or procedures as would normally be available to him.

Id. (emphasis added).

The *Deckert* court did not, however, expand the scope of remedies available under the securities laws. To the contrary, *Deckert* expressly recognized that its plaintiffs (unlike Plaintiff here) had asserted the requisite elements of a common law claim for equitable relief--including the ability to trace their sales proceeds into the hands of the defendant whose assets were sought to be seized. *Id.* at 288-289. Indeed, the *Deckert* court took pains to note that a claim in equity could only be maintained "[i]f petitioners' bill states a cause of action when tested by the customary rules governing suits of such character." *Id.* at 288. Thus, the court simply held that claimants under the Securities Act are entitled "to utilize any of the procedures or actions normally available to the litigant according to the exigencies of the particular case." *Id.* at 288 (emphasis added). It did not hold that the securities acts had created equitable remedies where none had existed before.

C.

Plaintiff's Characterization of Its Federal Securities Claims as "Legal" or "Equitable" in Nature is Irrelevant to the Court's Power.

It is also entirely irrelevant whether Plaintiff's statutory claims under the federal securities laws are labeled as being "equitable" or "legal" in nature, because such characterizations cannot answer the dispositive question: Whether the allegations pleaded in support of such claims also satisfy the "prerequisites" for, and therefore state a parallel claim for, equitable relief. As the Supreme Court explained in *Deckert*, the only relevant inquiry is whether the facts that are alleged in support of a federal securities cause of action also satisfy the traditional prerequisites of a claim for equitable relief. The governing rule is:

> If petitioners' bill states a cause of action [in equity] when tested by the customary rules governing suits of such character, the Securities Act authorizes maintenance of the [equitable] suit, providing the bill contains the allegations the Act requires.

Deckert, 311 U.S. at 288.

Here, Plaintiff has failed this test under any traditional equitable claim involving assets held by Defendants because Plaintiff has not alleged and cannot prove that Defendants have received any property or assets from Plaintiff as a result of any alleged fraud or other wrongful conduct. *See supra* Section I(C). No characterization or labeling of Plaintiff's statutory causes of action as "equitable" or "legal" in nature can alter this fact.

The fallacy inherent in Plaintiff's argument is that it relies on the proposition that, by the expedient of characterizing certain of its statutory causes of action as being "equitable" in nature, it can expand this Court's general equitable powers, under which the Court can now grant equitable relief that it otherwise would have no power to grant. This argument is contradicted by *Deckert*, it

ignores the limitations on the federal courts' general equitable powers as established by the Judiciary Act of 1789, and runs directly afoul of the Supreme Court's admonition in *Grupo Mexicano* that "the equitable powers conferred by the Judiciary Act of 1789 did not include the power to create remedies previously unknown to equity jurisprudence." *Grupo Mexicano*, 527 U.S. at 332.

D.

The Statutory Provisions Relied On Create Legal, Not Equitable, Remedies

Although it is irrelevant to the proper inquiry, the securities claims that Plaintiff has asserted, relating to the alleged insider stock sales, are not "equitable" in nature:

> We start with the basic proposition, which ultimately controls this case, that the appellees seek to recover money damages for violations of federal securities laws and state common law. The foregoing discussion of the factual background makes clear that the appellees' claims are legal, not equitable, in nature.

Rosen v. Cascade Int'l., Inc., 21 F.3d 1520, 1527 (11th Cir. 1994). Here, as in *Rosen*, Plaintiff's claims are purely legal.[9]

Plaintiff brought this action under sections 10(b), 20(a) and 20A of the Exchange Act [15 U.S.C. §§ 78j(b), 78t(a) and 78t-1] and Rule 10b-5 [17 C.F.R. §240.10b-5], and under sections 11 and 15 of the Securities Act [15 U.S.C. §§77k and 77o]. Plaintiff recited jurisdiction pursuant to 28 U.S.C. §1331 and §1337, and §27 of the Exchange Act [15 U.S.C. §78aa] and §22 of the Securities Act [15 U.S.C. §77v]. Complaint, ¶¶ 5 and 6. None of the statutory provisions relied on in the Complaint contain any language which creates a cause of action other than a damages claim, much less any language creating a constructive trust in Defendants' assets. Nor do the statutory

[9]The availability to Plaintiff of statutory legal claims for damages subjects Plaintiff to "the general rule that a court in equity should not act when the moving party has an adequate remedy at law." *In re "Ronfin" Series C Bonds Security Interest Litigation*, 182 F.3d 366, 373 (5th Cir. 1999); *see also Guaranty Trust Co. v. York*, 326 U.S. 99, 105 (1945)(discussing historic boundaries of federal equity jurisdiction, including absence of an adequate remedy at law), cited with approval in *Grupo Mexicano*, 527 U.S. at 318, 119 S.Ct. at 1968.

provisions relied on permit the pre-judgment seizure sought by Plaintiff. For convenience we summarize each cited provision briefly:

> Section 10(b) of the Exchange Act [15 U.S.C. §§ 78j(b)] prohibits use of "any manipulative or deceptive device or contrivance" but describes no specific remedy and no equitable remedy whatsoever.
>
> Section 20(a) of the Exchange Act [15 U.S.C. §78t(a)] imposes joint and several liability in certain circumstances, but makes no reference to equitable remedies, whether traditional (as would be required under *Grupo Mexicano*) or otherwise.
>
> Section 20A of the Exchange Act [15 U.S.C. §78t-1] creates liability to contemporaneous traders for insider trading. Under 15 U.S.C. §78t-1(a), a person who violates "shall be liable in an action" (emphasis added) – classic words for a legal, not equitable, remedy (*see Feltner*, discussed below). Under 15 U.S.C. §78t-1(b)(1), Congress set "the total amount of damages imposed" as not to exceed "the profit gained or loss avoided" in the violative transactions. Again, the operative word is "damages"–another classic word for a legal, not equitable, remedy. Subsection 15.U.S.C. §78t-1(b)(2), the "total amount of damages imposed" is to be diminished by amounts the defendant must "disgorge," pursuant to any court order obtained by the SEC under §78u(d) for the same transaction. Section 78u(d) is not pleaded and cannot be pleaded by the Plaintiff since it furnishes a remedy available only to the SEC. Section 78u(d) empowers the SEC (as opposed to a private litigant) to seek injunctive relief and to seek penalties including "the gross amount of pecuniary gain" and refers to funds which are "disgorged" as a result of such SEC action. This language clearly shows that Congress differentiated between the right of a *private litigant* to the legal remedy of *damages*, and the powers of the SEC to seek "disgorgement" through injunctive proceedings. Moreover, Section 20A grants a plaintiff no right to any particular assets of the defendant. Indeed, a private litigant's right to damages under 20A can be reduced in part or eliminated in whole if the SEC obtains an order of disgorgement for some or all of the insider trading profits, *id.* at 78t-1(b)(2), or if some other private litigant recovers the full amount of the defendant's insider trading profits under 20A before the first litigant can prosecute his claim to judgment. *Id.* at 78t-1(b)(2).
>
> Section 11 of the Securities Act [15 U.S.C.§77k] creates civil liability for false registration statements. Under subsection (a), a person acquiring such a security may "sue" liable persons. The measure of damages is set forth in subsection (e): the plaintiff may "recover such damages" as shall represent the difference between the amount paid for the security and the value at the time of suit, the price at which the security was sold before suit, or the value at which the security was sold after suit but before judgment. The remedy created is a damages remedy, not an equitable remedy. Moreover, Plaintiff's Section 11 claim is not relevant here because it relates to Enron's sale of bonds and not the alleged insider stock sales at issue here.

> Section 15 of the Securities Act [15 U.S.C. §§77o] makes "controlling persons" jointly and severally liable with persons liable under §77k (civil liability for false registration statement) or 77*l* (civil liability in connection with prospectuses and communications), again without reference to any equitable relief.

In *Feltner v. Columbia Pictures Television, Inc.*, 523 U.S. 340, 352, 118 S.Ct. 1279, 1287 (1998), the Supreme Court provided helpful guidance to be used in determining whether statutory remedies are legal or equitable in nature:

> We have recognized the "general rule" that monetary relief is legal, *Teamsters v. Terry, supra,* at 570, 110 S.Ct., at 1347-1348, and an award of statutory damages may serve purposes traditionally associated with legal relief, such as compensation and punishment. See *Curtis v. Loether*, 415 U.S., at 196, 94 S.Ct., at 1009 (actual damages are "traditional form of relief offered in the courts of law"); *Tull v. United States*, 481 U.S., at 422, 107 S.Ct., at 1838. "Remedies intended to punish culpable individuals...were issued by courts of law, not courts of equity"). Nor, as we have previously stated, is a monetary remedy rendered equitable simply because it is "not fixed or readily calculable from a fixed formula." *Id.*, at 422, n.7, 107 S.Ct., at 1838, n.7.

Feltner, 523 U.S. at 353, 118 S.Ct. at 1287. The underlying relief Plaintiff seeks here is clearly monetary relief, falling within the "general rule" that it is a legal claim, as recognized in *Feltner*.

Plaintiff's attempt to persuade this Court to impose a pre-judgment asset freeze falls directly within *Grupo Mexicano's* prohibition. It is an attempt to secure pre-judgment protection for the ultimate *legal* remedy Plaintiff seeks in this case. Since the ultimate relief sought here is legal damages, *Feltner*, 523 U.S. at 353, Plaintiff is not entitled to a pre-judgment freeze in aid of a legal remedy. In the words of the Eleventh Circuit:

> We repeat: preliminary injunctive relief freezing a defendant's assets in order to establish a fund with which to satisfy a potential judgment for money damages is simply <u>not an appropriate exercise of a federal district court's authority</u>."

Rosen, 21 F.3d at 1530. The *Rosen* court rejected a plaintiff's effort to seize assets on virtually identical facts in a claim arising under the federal securities laws. This Court should do likewise.

Conclusion

The opinion in *Grupo Mexicano* makes clear that Plaintiff is not entitled to a prejudgment seizure purely to secure their right to recover a legal judgment. Nor is Plaintiff entitled to a prejudgment seizure if, as here, it has failed to state a claim for equitable relief "tested by customary rules governing suits of such character." Plaintiff's demand for prejudgment seizure should be denied.[10]

[10]Defendant Ken L. Harrison has new counsel located in Oregon, who has indicated that Mr. Harrison joins in this brief.

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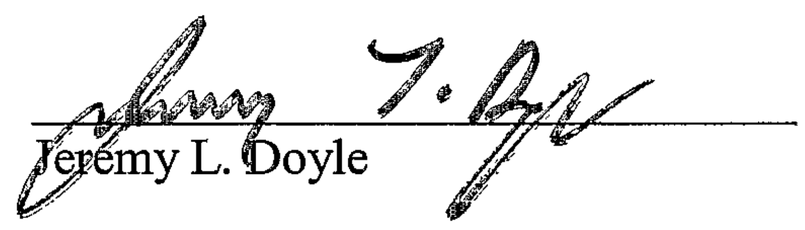

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The Exhibit(s) May

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